

Is your internal audit activity doing what you
and your board of directors want?
If not, what steps are you taking to change it?

BETTER Internal Audit Leads to BETTER Controls

By Robert B. Hirth Jr.

Many think of internal controls as the unique combination of people, processes and technologies created in organizations. However, to ensure strong controls are established within organizations, it is important to consider questions such as:

- ☐ What activities further improve control in our organization today and in the future?
- ☐ How can we enable events that will improve our controls over time?
- ☐ How do we build and maintain a mindset and culture that complements, as well supports, our firm's controls?
- ☐ How can we intersperse managers throughout the organization who understand, appreciate and

help further a well-controlled environment?

An effective internal audit activity within an organization will help answer these questions and achieve the desired goals around them.

Indeed, companies with the best internal audit functions — those that employ leading practices and are in sync with the expectations of, and strategic objectives defined by, management and boards of directors — generally have better controls.

This does not mean that simply having an internal audit activity ensures good controls. Rather, a high-performing internal audit activity creates a higher probability of better controls. Conversely, an internal audit function that per-

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forms poorly does not and is unlikely to foster the development and maintenance of strong internal controls.

While internal control is defined by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), internal auditing is defined by The Institute of Internal Auditors (IIA) as an:

“independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.”

Companies that create an internal audit function that delivers on this definition will create a highly valuable asset. In fact, when combined with the activities of better internal audit functions described below, the result is a key competitive advantage: a high-performing internal audit function that helps to properly validate and continuously improve controls and serves as a vital source of management talent that delivers future leaders for the organization.

The attributes of what exactly defines a “better” internal audit function are discussed below.

Better People

This is where an effective internal audit function begins and often ends. A good team of highly qualified professionals from throughout the organization — not just “career” internal auditors, but professionals

from accounting, finance, information technology, operations and other departments — who are committed to the mission and objectives of the internal audit function will consistently deliver over and above an average team.

Better-performing internal audit functions leverage their status in the organization and promote proven career and leadership positions outside of internal audit to attract better people.

Perhaps more than at any time before, there are exceptional career growth and development opportunities for professionals who become part of the organization's internal audit function, either on an interim or permanent basis.

Today's internal audit profession requires innovative thinkers who can meet a wide range of challenges related to governance, risk and compliance (GRC). They must be ready to explore new technologies, identify and help mitigate emerging risks and develop creative solutions to complex business problems.

Professionals who meet these challenges are able to enhance their career prospects significantly. With the knowledge they acquire about the organization, these individuals often transfer from the internal audit function to other influential roles in the enterprise, and are, in fact, encouraged to do so by their leadership and senior management. In short, their knowledge is vital and useful to the organization in ways that extend far beyond performing audits.

Better Risk Assessment

Risk assessment remains at the heart of internal audit. It defines the focus as well as the effort of the internal audit staff. Getting it right through a comprehensive risk assessment will drive better results, achieve greater efficiencies and cover the important things that either add or preserve value in the organization.

To get it wrong means wasted time and effort, potentially major risks and issues slipping through the cracks and a poor sense of the organi-

zation's control environment. Leading internal audit activities make this process their very best.

Accordingly, they truly and deeply understand the organization's business model, its drivers, major projects and key objectives.

Better internal audit functions collaborate with management and the board to develop an effective process for the enterprise to facilitate the identification of risks that are most relevant to achieving its strategic objectives.

Customized risk models are available that establish a common language for discussing business risks. Such a model can serve as a basis for codifying, mining and aggregating risk data to make the evaluation and tracking of risks much more effective and efficient.

Better Use of Technology

Internal auditors can gain tremendous leverage, improve coverage and achieve better validation through the use of technology. Better-performing internal auditors use technology tools to monitor operations, scan key performance indicators and interrogate databases rather than relying solely on sampling random groups of transactions.

Information technology security, business continuity, transaction accuracy, data integrity, segregation of duties and continuous auditing and monitoring are examples of where technology is being employed in the audit process to do more — better, faster and cheaper.

As further evidence of technology's importance in the auditing process, Protiviti Inc. recently conducted a survey of chief audit executives and other internal auditing professionals to assess their current capabilities and areas for improvement in a number of categories, including audit-process knowledge.

One notable finding from the survey, *2008 Internal Audit Capabilities and Needs*: computer-assisted audit techniques was the highest-ranking area identified as being in need of improvement.

Computer-assisted audit technologies are becoming increasingly prevalent as companies automate and streamline internal audit processes. More firms also are seeking to alleviate some of the burden on internal audit personnel who, over the past few years, have been tasked with monitoring continuously for fraudulent activity and internal control weaknesses — many times on a less than fully automated basis.

Because internal auditors have been so focused on such activities, they have devoted less attention to many day-to-day — yet vital — general internal control-related tasks and other traditional internal audit responsibilities.

Computer-assisted audit techniques enable real-time, automated independent testing of critical enterprise data. But, as is the case with most technology, there can be a significant initial investment involved, as well as training and implementation time.

Organizations that are committed to achieving better controls through improved internal audit activities are making this investment in terms of budget, training and implementation.

Better Techniques Add Value, Increase Efficiency

The better internal audit functions are adopting concepts such as Six Sigma, ISO 9000, balanced scorecard, continuous improvement and others. They're also considering these concepts in their recommendations and helping their organizations adopt the philosophies and management systems.

In addition, self-assessment techniques are being used to achieve better coverage and resource leverage as well as to impart more knowledge among all employees about risks and controls in the organization.

Better Overall Process

Leading internal audit activities have studied, evaluated and honed their own processes to near perfection, ensuring they are efficient and highly productive. The best functions measure themselves relentlessly in areas

such as cycle time, recommendation status, customer feedback and individual productivity.

These groups adhere to The IIA's *International Standards for the Professional Practice of Internal Auditing*, including having an independent quality assessment review at least every five years. Furthermore, these internal functions seamlessly train and mentor new staff members who rotate into the internal audit function so that all activities and services continue at a high level of performance.

Better Risk Leadership

The best internal audit activities and their leaders are taking a proactive position as to how they can expand their responsibilities to ensure they have input, provide oversight and add value to GRC initiatives. In many instances, internal audit is assuming an initial lead role in the development of this area within the organization.

The current challenges organizations are dealing with relate to the types of tools that should be adopted to manage overall GRC initiatives, many of which seek to aggregate risk-related information across the enterprise from areas such as compliance, regulatory, risk management, quality and internal audit.

Better Knowledge of Limitations

Today's internal audit leaders know they cannot be all things to all people. They work closely with management and the board of directors to define their roles in a way that they truly can be effective and deliver on their mandate.

They recognize, realize and discuss risks that are out of the organization's control, but also have a clear view of those risks that are within their control and that can be rejected, mitigated, reduced, transferred or controlled more effectively.

Further, they recognize that with the fluctuating workloads and demands common within internal audit functions over the course of a fiscal year, they never should have all of the resources they need all of the time. Instead, they should proactive-

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ly, judiciously and thoughtfully leverage outside resources to add even more value and expertise in their capacity as a vital link in the internal control chain.

After assessing the factors that differentiate "better" internal audit activities from lower-performing ones, consider your firm's internal audit function and ask:

☐ Do you have an internal audit activity that enables better controls in your organization? If not, is now the time to consider one?

☐ How can your internal audit activity become better and raise the probability of the internal controls not only improving today, but being continuously monitored and, if necessary, enhanced over time as the organization grows and evolves?

Then, and perhaps most importantly, consider whether your internal audit activity is really doing what you and the board of directors want it to do. If it is not, then what steps are you taking to change it?

This final point is key because the primary role of an internal audit activity is to work to achieve the strategic objectives you define. When this happens, better controls throughout the organization will result.

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